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SUBJECT: GERMAN CABINET RETREAT FOCUSES ON CLIMATE AND ENERGY, FOREIGN INVESTMENT, AND SUBPRIME CRISIS

¶1. (SBU) Summary: German Chancellor Angela Merkel emerged from the August 23-24 Federal Cabinet retreat with consensus among the parties in her Grand Coalition Government on a 50-point program designed to sustain Germany's economic upturn. No signs of coalition cracks appeared. The program includes a 30-point plan on energy and climate change and focuses on balancing the federal government budget, protecting key German industries from "hostile" foreign investment, greater transparency in financial markets, and education and immigration strategies to address a shortage of skilled labor. The climate change plan calls for improved cooperation with the United States on carbon capture and sequestration, renewables, and energy efficiency. Concern about the sub prime crisis in the United States prompted calls for investigations of rating agencies and for greater regulation of hedge funds. End Summary.

¶2. (SBU) During an August 24 press conference, Chancellor Angela Merkel (CDU) and Deputy Chancellor/Labor Minister Franz Muentefering (SPD) unveiled the results of the August 23-24 Cabinet retreat at Meseberg Castle in Brandenburg. The 50-point program, titled "Upturn - Participation - Prosperity," is designed to guide the Grand Coalition government up until the 2009 elections. The Coalition, at least on the surface, showed no signs of discord, as participants focused on domestic issues. Merkel and Muentefering began the press conference by highlighting the Grand Coalition's accomplishments in its first two years, focusing special attention on Germany's economic upturn and declining unemployment rate. Merkel said the Grand Coalition would focus on extending and expanding the economic upturn. "We do not want to leave anyone behind," Merkel said. Muentefering stressed the need to secure growth and prosperity in order to maintain a "social balance." The agreement was criticized by most opposition parties as lacking substance.

GERMANY'S 30-POINT CLIMATE PROTECTION PROGRAM

¶3. (U) Among the few concrete measures adopted by the Cabinet was a comprehensive 30-point climate protection program aimed at meeting Germany's ambitious goals to reduce CO2 emissions.

In order to achieve the EU-wide 20 percent reduction target by 2020, Germany needs to reduce its GHG emissions by 40 percent of the 1990 base. Although the full funding requirements are not yet known, the Environment Ministry's climate change budget was increased from the current EUR 700 million to EUR 2.6 billion in 2008. The German Government anticipates EUR 400 million will be raised by the sale of emissions trading certificates.

¶4. (U) Whereas some of the measures such as vehicle emissions

restrictions are still under discussion in the EU, others, such as vehicle-specific taxes, fall within the jurisdiction of the (German) federal states. The Federal Government will introduce legislation for those measures which can be regulated nationally in the fall. Environment experts and NGOs criticized the program as lacking ambition and effectiveness. The Environment Ministry acknowledged that these measures are expected to reduce emissions by 35-to-36 percent and expects federal states and local authorities to provide the final 5 percent savings to reach the 40 percent goal.

15. (U) The package targets public and private buildings, transportation, and the energy sector. It includes clean coal measures and improved cooperation with the U.S. on carbon capture and sequestration, renewables, and energy efficiency. Planned measures include:

- a 30 percent hike in energy savings requirements for new buildings constructed after 2008, with a further 30 percent savings requirement by 2012,
- expansion of a market incentives program for refurbishing older buildings,
- a renewables share of 15 percent for heating in new buildings,
- legislation to promote commercial uptake of carbon capture/sequestration and zero-emissions coal power plants,
- increasing the renewables share of power generation from the current 14 percent to 25-to-30 percent by 2020,
- replacing 10 percent of gas consumption with biofuels from biogas by 2030, and
- doubling the CHP share in power generation to 25 percent by 2020 with the aid of a EUR 750 million incentive program.

16. (U) Measures in the transportation sector include advocating a 130 gram emissions limit for automobiles

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adjusted to engine size, revamping the vehicle tax, a truck levy to reward low CO2 emissions and a target of 17 percent bio fuel in gasoline by 2020, and inclusion of aviation emissions in the EU's emissions trading system.

PROTECTING KEY GERMAN INDUSTRIES

17. (U) Merkel announced the formation of a working group comprised of representatives from the Finance and Economics ministries charged with developing measures to protect strategic German industries from investment funds controlled by foreign governments. Merkel stressed that Germany had no intention to close its borders to potential investors but was looking for a mechanism similar to those used by the United States, Great Britain, and France to protect key industries from potential hostile foreign engagement. Such measures, she said, would be in accordance with WTO principles and would also not violate the EU's internal market rules.

18. (U) The cabinet agreed to review Germany's legislation on foreign investment to determine whether German law allows for the possibility of implementing certain protective measures, such as a turnover-threshold beyond which a target company would be subject to government control. Another tool the cabinet agreed to consider was the creation of a special "fund" of (German) banks and industry to counter activities of foreign, state-owned funds on the German market. Merkel said that she would seek a dialogue with French President Sarkozy about introducing such protective measures on the EU level, or as part of the EU's Lisbon Process for global competitiveness.

RENEWED CALL FOR GREATER TRANSPARENCY OF FINANCIAL MARKETS

19. (U) Merkel and Muentefering said the impact of the U.S. sub prime market turmoil on the financial system demonstrated the need for an investigation of rating agencies and justified a renewed call for greater "transparency" in

financial markets. Merkel said Germany would use the remainder of its G-8 Presidency and the September IMF meeting as platforms for discussing the matter. Of particular concern to the German government are the financing mechanisms of international hedge funds. "Recent (market) turbulence shows the significance that such regulation would have," Muentefering said.

BALANCED BUDGET AS OVERARCHING GOAL

¶10. (U) Chancellor Merkel reiterated the Coalition's goal - as set out by Finance Minister Peer Steinbrueck (SPD) - to achieve a balanced budget by 2011. Merkel stressed that further budget consolidation would be necessary to give the government sufficient room "to steer the political course." She emphasized that none of the new spending measures agreed in Meseberg would result in extra costs or go beyond what the government had already earmarked in its budget. Merkel also ruled out the possibility of any reduction in taxes before 2010, but explicitly left the door open for a possible lowering of non-wage-labor costs, e.g., unemployment insurance premiums, in order to reduce labor costs.

COPING WITH A SHORTAGE OF SKILLED LABOR

¶11. (U) To cope with the growing shortage of skilled workers in Germany, the cabinet decided to improve qualification and retraining programs for German citizens and to grant foreign students and engineers easier access to the German labor market, as early as November 1. The cabinet agreed that engineers of new (eastern) EU member states with certain special skills, such as electrical and mechanical engineering, will be permitted to work in Germany without providing - previously obligatory - proof to an employment office that no comparable German specialist is available to fill a certain position.

¶12. (U) Moreover, foreign students who have graduated from a German university may work in their acquired profession without restrictions for up to three years in Germany. The cabinet tasked the Ministries of Labor and Education to develop a comprehensive immigration program (a points-based immigration system for skilled workers like that in Canada is reportedly under consideration). The new plan also includes a provision to lower the unrealistically high income requirement for immigrants. Under current practice, skilled professionals are only given permission to come to Germany if they can prove they will earn an annual salary of EUR 85,000 euros. The Education Ministry advocates reducing the limit to EUR 40,000 - 60,000 euros, a figure that many business

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leaders insist is still too high.

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